

COMMONWEALTH OF AUSTRALIA

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Family Name	
Given Names	
Student Number	
Teaching Period	Semester 1, 2016

FINAL EXAMINATION	DURATION
ACT504 – Auditing	Reading Time: 10 minutes Writing Time: 180 minutes

INSTRUCTIONS TO CANDIDATES

1.1 The examination has 3 sections.

Section A: Suggested Time:	Multiple Choice Questions: Answer ALL questions 40 marks 80 minutes
Section B: Suggested Time:	Short Answer Questions: Answer ALL questions 40 marks 70 minutes
Section C: Suggested Time:	Case Study Questions: Answer ALL questions 20 marks 30 minutes

Section A must be answered on the Multiple Choice Answer sheet provided in this examination paper and must be handed in with your answer booklet. Please ensure that your name and student number are clearly indicated on your Answer Sheet and at the top of this examination paper.

Section B and Section C are to be answered in the Answer booklet provided.

- 1.2 Note that questions **ARE NOT** of equal value.
- 1.3 Read **ALL** questions carefully.

EXAM CONDITIONS

You may begin writing from the commencement of the examination session. The reading time indicated above is provided as a guide only.
This is a RESTRICTED OPEN BOOK examination
No calculators are permitted
No handwritten notes are permitted
Hard copy, unannotated English translation dictionary only

ADDITIONAL AUTHORISED MATERIALS	EXAMINATION MATERIALS TO BE SUPPLIED
Relevant Legislation (Unannotated)	1 x 16 Page Book 1 x 4-Multiple Choice Answer Sheet

**THIS EXAMINATION IS PRINTED
DOUBLE-SIDED.**

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Section A
Multiple Choice Questions
Total No of Marks for this section: 40

This section should be answered on the Multiple Choice Answer Sheet provided. Please ensure that your name and student number have been written on the Answer sheet and place in the completed answer Booklet.

Each question carries 1 mark. Suggested Time allocation for Section A: 80 mins

Section B
Short Answer Questions
Total No of Marks for this section: 40
Answer 4 of 4 questions

This section should be answered in the Answer Booklet provided.

Marks for each question are indicated. Suggested Time allocation for Section B: 70 mins

Question 1: (10 marks)

You are a newly qualified accountant who works for the audit firm Harrison Ford & Co. You have been approached by a potential new client, Calista Electronics Pty Ltd, who is looking for an audit firm to carry out an audit on its annual financial report prepared in accordance with the Corporations Act. The managing director, Calista Flockhart, is not sure exactly what an audit involves and what are the responsibilities of the auditor.

REQUIRED:

Prepare notes for a meeting with Calista Flockhart which identifies the responsibilities of the auditor and the responsibilities of management.

(10 marks)

The notes should cover the following:

- Distribution of the annual report to shareholders.
- Delivery of the audit report to the entity.
- Obtaining and evaluating evidence concerning the financial report.
- Preparation and presentation of the financial report.
- Maintaining adequate internal controls.
- Testing internal control procedures.
- Expressing an opinion on the financial report.
- Selecting appropriate accounting policies.
- Ensuring the financial report is presented in accordance with standards.
- Performing test of controls.

Question 2: (10 marks)

You are currently planning the audit of Twentyfour Seven Pty Ltd (TSPL), a large proprietary company that operates a small chain of convenience stores. You are in the process of developing an understanding of its objectives and strategies and the related business risks.

Competition in this sector is intense, with major supermarket chains aggressively purchasing smaller rivals and discounting products below cost in order to increase market share. In order to compete, TSPL has been forced to offer value-added services such as complimentary coffees based on a loyalty scheme.

While these strategies have helped to maintain its customer base, its gross margins have dropped by 10%. In an effort to increase profits, TSPL has recently focused on expanding the products available in each store. However, these items have achieved only limited acceptance to date among TSPL's customers and stock obsolescence is high.

All of TSPL's premises are leased. Two of the leases are due to expire prior to the end of the current financial year. In both cases, the land on which the premises are situated has been re-zoned as residential. Due to "prior use" legislation, this does not prevent the premises from being used as a supermarket in the future. However, it does mean the land's value has increased and, on this basis, the lessor is demanding a 50% increase in rent.

TSPL is also experiencing difficulties with two of its major suppliers, who have withdrawn their volume rebates and reduced payment terms from 30 to 14 days. In addition, TSPL has recently initiated legal action against a major supermarket chain for anti-competitive behaviour and predatory pricing.

REQUIRED:

(a) Identify five (5) business risks, as per ISA 315, which may lead to the risk of material misstatement at the financial statement level for TSPL. (5 marks)

(b) For each business risk you identified in (a) above, describe how it may lead to the risk of material misstatement at the financial statement level. (5 marks)

You may wish to present your answer to (a) and (b) using the following table:

<i>(a) Business risk</i>	<i>(b) How it might lead to risk of material misstatement</i>

Question 3: (10 marks)

Listed below are ten substantive procedures:

1. Select a sample of non-current assets and sight them.
2. Review the income statement for unusual differences in the balances recorded for this year and last year.
3. Select a sample of invoices and ensure that they have been properly recorded in the sales ledger.
4. Trace the last inventory received before the year-end to the inventory listing.
5. Review the adequacy of the company's allowance for doubtful debts.
6. Ensure that interest paid on the bank loan is correct by multiplying the interest rate by the outstanding principal for each month of the year.
7. Send a letter to the bank to confirm a loan taken out by the company during the year.
8. Attend the year-end stocktake and perform test counts on a sample of stock items.
9. Review all invoices received for one month after the year-end to ensure that they do not relate to the current year.
10. Calculate the accounts receivable turnover and compare with previous year's turnover.

REQUIRED:

- (a) For each test, indicate what type of substantive procedure to which it relates (analytical review, tests of details of balances or tests of details of transactions). (5 marks)**
- (b) Give one assertion to which each test relates. (5 marks)**

Question 4: (10 marks)

The financial year of Justice League Pty Ltd ended on 30 June 2015. Your auditor's report was signed on 25 August and the financial statements were issued on 10 September. Listed below are events that occurred or were discovered after the end of the financial year. Assume that each has a "**material**" effect on the financial statements.

1. 15 September — A fire burnt down one of Justice League's warehouses, resulting in a loss of 30% of the inventory that was on hand at that date.
2. 30 September — You discovered that Bruce, a debtor of Justice League, went bankrupt on 15 July. Sales to Bruce were all made before the end of the year.
3. 1 August — A lawsuit was filed against Justice League for damages that allegedly occurred before 30 June. In the opinion of Justice League's lawyers, there is a danger of a significant loss.
4. 15 August — You discovered that Clark, a debtor of Justice League went bankrupt on 10 August. The most recent sale had taken place on 25 May and no transactions had occurred since that date.
5. 1 September — You discovered that a legal action commenced against Justice League in relation to a faulty product sold in May 2015.

REQUIRED:

(a) Indicate your responsibilities for each of the above events.

(5 marks)

(b) Indicate the type of disclosure (if any) you would recommend in relation to each of the six events.

(5 marks)

Section C Case Study Questions

Total Number of Marks for this section: 20

This section should be answered in the Answer Booklet provided.

Marks for the question is as indicated. Suggested Time allocation for Section C: 30 mins

Section C (20 marks)

Background information

Darwin Playtime Ltd (DPL) is a toy manufacturer. DPL has factories across the country and its customer base includes retailers, as well as individuals, to whom direct sales are made through their website. You are an audit senior at Raul David & Associates and you are currently reviewing documentation of DPL's internal controls in preparation for the interim audit.

DPL's website allows individuals to order goods directly and full payment is taken in advance. Currently the website is not integrated into the inventory system and inventory levels are not checked at the time when orders are placed.

Goods are delivered via local couriers; however, the couriers do not always record customer signatures as proof that the customer has received the goods. Over the past year, there have been customer complaints about the delay between sales orders and receipt of goods. DPL has investigated these complaints and found that, in each case, the sales order had been entered into the sales system correctly, but was not forwarded to the despatch department for fulfilling.

DPL's retail customers undergo credit checks prior to being accepted and credit limits are set accordingly by sales ledger clerks. Neither the sales area managers nor the sales director are involved with this process. These customers place their orders through one of the sales team, who decides on sales discount levels.

Raw materials are purchased from a wide range of suppliers. As a result of staff changes in the purchase ledger department, supplier statement reconciliations are no longer performed. Additionally, changes to existing supplier details or inclusion of new supplier details in the purchase ledger master file can be undertaken by purchase ledger clerks, as well as supervisors.

In the past six months, DPL has changed part of its manufacturing process and as a result some new equipment has been purchased. However, there are now considerable levels of plant and equipment that are now surplus to requirement. Purchase requisitions for all new equipment have been authorised by production supervisors and little has been done to reduce the surplus of old equipment.

REQUIRED:

- a) **Identify five (5) deficiencies in the internal controls of DPL. Explain how a business risk arises from each deficiency.** (10 marks)
- b) **Describe a control which DPL could implement to address each of these deficiencies.** (5 marks)
- c) **Design a test of control Raul David & Associates would perform to assess if each of those controls identified in (b) above is operating effectively.** (5 marks)

You may wish to present your answer in a table format, as follows:

<i>(a) Deficiency</i>	<i>Explanation</i>	<i>(b) Control</i>	<i>(c) Test of control</i>